IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 104 of 1985

For Approval and Signature:

Hon'ble CHIEF JUSTICE MR DM DHARMADHIKARI
and
Hon'ble MR.JUSTICE A.R.DAVE

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

1 to 5 NO

JJJJ

Date of decision: 26/09/2000

ORAL JUDGEMENT

(per D.M. Dharmadhikari, C.J.)

This is a reference under sec. 256(1) of the Income-tax Act, 1961 at the instance of the revenue. The assessee, despite service of notice, has failed to appear and is, therefore, not represented.

2. The learned counsel appearing for the department points out that the question raised is squarely covered by the decision of the Supreme Court in Tuticorin Alkali Chemicals and Fertilizers Ltd. v. CIT reported in (1997) 227 ITR 172.

3. The few facts which are to be mentioned are that the assessee, in the assessment years 1978-79 and 1979-80, had received interest income from the funds borrowed from different financial institutions for running the business of the assessee. In the assessment years in question, the assessee had not commenced its business. It had earned interest income from the amount borrowed and had to pay interest on the borrowed amount. It is on these facts that the following question of law came to be referred to this court :

"Whether, on the facts and in the circumstances of the case, the ITAT was right in law in coming to the conclusion that the interest received by the assessee should be adjusted against the interest payable by it and that the rest of amount of interest be allowed to be capitalised?"

4. The learned counsel for the department took us through the decision of the Supreme Court in the case of Tuticorin Alkali Chemicals (supra). On perusal of the decision of the Supreme Court, we find that the point raised is squarely covered by the following observations of the Supreme Court :

"Interest income is always of a revenue nature, unless it is received by way of damages or compensation. If a person borrows money for business purposes but utilises that money to earn interest, however temporarily, the interest so generated will be his income. This income can be utilised by the assessee whichever way he likes. He may or may not discharge his liability to pay interest with this income. Merely because it was

utilised to repay the interest on the loan taken by the assessee, it did not cease to be h is income. When the question is whether a receipt of money is taxable or not or whether certain deductions from that receipt are permissible in law or not, the question has to be decided according to the principles of law, and not in accordance with accountancy practice. Accounting practice cannot override section 56 or any other provision of the Income-tax Act.

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The company could not claim any relief under section 70 or section 71 since its business had not started and there could not be any computation of business income or loss incurred by the assessee in the relevant accounting years. In such a situation, the expenditure incurred by the assessee for the purpose of setting up its business could not be allowed as deduction, nor could it be adjusted against any other income under any other head. Similarly, any income from a non-business source could not be set off against the liability to pay interest on funds borrowed for the purpose of purchase of plant and machinery even before commencement of the business of the assessee."

5. In view of the clear pronouncement of the Supreme Court quoted above, the question is answered in the negative, in favour of the revenue and against the assessee.

The reference is disposed with no order as to costs.

(D.M. Dharmadhikari, C.J.)

(A.R. Dave, J.)

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